

**State of Washington
Department of Labor and Industries
Decision Package**

Decision Package Code/Title	9E	Other Fund Adjustments - Fair Distribution of Administrative Costs
Budget Period	2005-07	FY06 Supplemental Budget
Budget Level	M2	Maintenance Level

Recommendation Summary Text

L&I requests a change in appropriation level to distribute indirect costs to more equitably and fairly reflect the costs of support to L&I direct service programs. This proposal doesn't change overall agency costs or administrative costs. In addition, the department is requesting the partial transfer of electrical, asbestos and pressure vessel revenue back to their respective dedicated accounts from the General Fund. This will give these funds a greater capacity to absorb the effects of this package along with the previous impacts of indirect cost allocation during Phase I and Phase II implementation.

Fiscal Detail:

Staffing (B6):

TOTAL FTEs

FY 2006	FY 2007	TOTAL
0.0	0.0	0.0
0.0	0.0	0.0

Operating Expenditures:

001-1 General Fund State
02V-1 Public Safety & Education Account
03B-1 Asbestos Fund
095-1 Electrical License Account
163-1 Worker/Community Right to Know Account
234-1 Public Works Administration Account
608-1 Accident Fund-State
609-1 Medical Aid Fund-State
885-1 Plumbing Certificate Account
892-1 Pressure Systems Safety Account

TOTAL Expenditures

FY 2006	FY 2007	TOTAL
0	13,000	13,000
0	139,000	139,000
0	0	0
0	122,000	122,000
0	(17,000)	(17,000)
0	256,000	256,000
0	(274,000)	(274,000)
0	(274,000)	(274,000)
0	12,000	12,000
0	23,000	23,000
\$0	\$0	\$0

	FY 2006	FY 2007	TOTAL
Revenue:			
001 General Fund 06-22	(1,052,000)	(1,269,000)	(2,321,000)
095 Electrical Account 06-21	909,000	1,112,000	2,021,000
03B Asbestos Account 06-21	29,000	27,000	56,000
892 Pressure Systems Safety Acct 06-21	114,000	130,000	244,000
TOTAL Revenue	\$0	\$0	\$0

Package Description:

In the Washington State Auditor's Office 2002 Statewide Accountability Report, L&I received an audit finding stating that "The Department of Labor and Industries did not allocate indirect costs equitably among its programs and funds" for the Administrative Services program. The result, according to the report, is that the agency was in violation of the Local Government Accounting Statute, RCW 43.09.210, which precludes one fund from benefiting at the expense of another fund.

In response to the finding, the L&I identified cost accounting expertise outside the agency to help develop a sound, equitable method to allocate indirect costs across three programs (Administrative Services, Information Services and Legal Services). Working closely with an independent consulting firm, an indirect cost allocation policy and model was developed to equitably allocate indirect costs to the programs that benefit from indirect services.

The department implemented this cost allocation policy by:

- Allocating costs based on annual allotments for appropriated funds and the cash flow forecast for non-appropriated funds. Expenditures used as the basis for this annual allocation are the 2005-07 allotments as approved by OFM.
- Allocating costs across the programs or sub-programs based on the approved funding splits within the program/subprogram.
- Updating the cost allocation model annually to reflect increases, decreases and changes to program areas.
- Updating the cost allocation model annually to reflect organizational or budget structure changes.
- Identifying costs for services that benefit one program and charging to that program directly. Those costs are not allocated out across all programs and funds. Direct charging for services such as tuition reimbursement will be based on the average of the actual costs reported for the past two fiscal years. Direct charging legal services is based on actual services received by program.

The indirect cost allocation policy was implemented in two phases over two fiscal years. Phase I implementation began on July 1, 2004, utilizing the new cost allocation model for the Administrative Services Program. The results of Phase I were approved by the 2004 Legislature as a net zero decision package.

Phase II implementation began on July 1, 2005 and built on the Phase I allocation of Administrative Services to include indirect costs from the Information Services Program and indirect costs from the Legal Services Program in the 2005-07 Biennium.

The results of Phase II were approved by the 2005 Legislature as a net zero decision package. The only change made to that request was that the Accident Account and the Medical Aid Account were used instead of the Public Works Administration Account because the latter account did not have the fund balance to accommodate the proposed expenditure increase.

This decision package realigns the Fiscal Year 2007 charges to the funding sources based on the impact of that allocation. This budget request will not increase the overall expenditures within the agency but will redistribute the charges for indirect services in an equitable manner across all funding sources. Based on our current revenue estimates, this proposal can be accomplished utilizing fund balances within those funds managed by the agency with the exception of the Public Works Administration Fund. This fund is projected to be in a fund balance deficit prior to the implementation of this proposal. Proposed legislation is included in department's legislative request to address this issue. This proposal was submitted separately.

In addition, the department is requesting the partial transfer of electrical, asbestos and pressure vessel revenue back to their respective dedicated accounts from the General Fund. The requested transfer is the equivalent of Phase I, Phase II and the update for this year of the impacts of the indirect cost allocation to these funds. This will give these funds a greater capacity to absorb the effects of this package and the future impacts of indirect cost allocation. These revenues were transferred by the Legislature during the 2003 Legislative Session as part of larger fund sweep to the General Fund. The transfer would be as follows:

- Electrical Account – \$2,021,000
- Asbestos Account – \$56,000
- Pressure Vessel Systems Account – \$244,000
- General Fund – (\$2,321,000)

Although there is an impact to the Farm Labor Fund of \$3,000, for the purposes of this request it has been added to the Accident and Medical Aid Funds. L&I has a total appropriation of \$28,000 from the Farm Labor Account. It has stayed this amount for several biennia. Previous budget requests for additional appropriation authority from the Farm Labor Account resulted in a subsidy, instead, from the Accident and Medical Aid Funds. This decision package request is consistent with that trend.

Narrative Justification and Impact Statement

This decision package supports the following Priorities of Government:

Improves the quality and productivity of our workforce by returning unemployed workers to work and making the workplace safe by facilitating case management and enforcement notifications; compliance; case documentation; and two-way client communication (POG Statewide Result 2);

Improves the health of Washington citizens by facilitating payment of medical expenses for workers' compensation claims (POG Statewide Result 4);

Improves security of Washington's vulnerable children and adults by facilitating eligibility determination and payments to victims of crime (POG Statewide Result 5);

Improves the economic vitality of businesses and individuals by maintaining a healthy business climate by facilitating case management and enforcement notifications; compliance documentation and two-way client communication in employment standards, prevailing wage and contractor registrations (POG Statewide Result 6);

Improves the safety of people and property by preventing accidents and prepares for emergencies by facilitating enforcement notifications, contractor certifications, pressure vessel certifications, compliance documentation and two-way client communication (POG Statewide Result 8);

Strengthens government's ability to achieve its results efficiently and effectively with efficient client-direct communication but would be diminished if client and other mail communication costs were not fully funded (POG Statewide Result 11).

This proposal supports all Labor and Industries' activities.

Performance Measure Detail:

L&I Goal to which this change is tied:

Administering one of the premier workers compensation organizations in the nation in quality of service, benefits and costs.

Performance Measure Changes:	Incremental Changes	
	<u>FY 2006</u>	<u>FY 2007</u>
Outcome Measures:		
Output Measures:		
Efficiency Measures:		

Statement of Expected Results:

Agency indirect costs are fairly and equitably shared amongst the direct service programs.

Reason for change

The department is responding to a State Auditor finding that the agency was in violation of the Local Government Accounting Statute, which precludes one fund from benefiting at the expense of another fund. Indirect costs are not allocated properly across the various other funds within the agency. In addition, this package will respond to the Joint Legislative Audit and Review Committee recommendation issued in December 1998 that the department should develop a system of allocating indirect costs among funding sources.

The partial return of the Electrical Account, Pressure Systems Safety Account and the Asbestos Account revenue will give those programs greater flexibility in gradually absorbing the impacts of the indirect cost allocation for those funds.

Impact of the change on clients and services

L&I has developed an equitable and fair process to allocate “indirect” costs or administrative costs such as personnel, payroll, accounting, budget, information services, legal services, etc. The agency will distribute costs to more clearly reflect usage of indirect services. This will allow the agency to develop unit costs for services that reflect the full costs of the service. These changes have a potential impact on some of the dedicated funds appropriated to the agency. This realignment proposal helps the stakeholders paying the fees into these accounts better understand that “their” revenues are being spent efficiently and properly.

Other impacted programs/divisions/regions

This is an agency wide issue that affects the fund balance of all of the funds appropriated to L&I. Some of these funds are administered by other state agencies such as General Fund-State and Public Safety and Education Account. The Right to Know Fund is administered by L&I but is appropriated among several other state agencies.

Relationship to capital budget

None

Required changes to existing RCW, WAC, contract or plan

The passage of 2006 department request legislation to eliminate the 30 percent transfer to General Fund of prevailing wage revenue is critically important to ensure continued levels of program services and maintain a solvent fund balance in the Public Works Administration Account. If the transfer is not eliminated, the program will be forced to reduce expenditures and service delivery to offset that funds share of allocated indirect costs.

Alternatives explored by agency

The agency explored several options in response to the State Auditors Office finding:

- 1) Do nothing and continue to receive audit findings. This is not a viable alternative and places the agency and its executives in legal jeopardy.
- 2) Seek an exemption from the Local Government Accounting Statute. This would be an appealing option for the stakeholders of the agency’s smaller dedicated funds that are affected by this decision package. However, the workers’ compensation stakeholders would consider this as a continued subsidy of employer premiums to non-worker compensation related activities. No other state agency has an exemption from this section of the Local Government Accounting Statute.
- 3) Manage the fund implications of the model internally and not seek legislative appropriation changes. This is not a viable option for the smaller dedicated funds of the agency. Direct services in the programs funded by these accounts would be substantially reduced while the fees for these services would remain static.

Budget impacts in future biennia

These costs are all on going. The cost allocation model will be updated annually and adjustments will be submitted via the budget process each year.

The return and transfer of revenue for Electrical, Asbestos and Pressure Systems Accounts would also be on going. The amount of the requested transfer is based on the effect of the cost allocation model on the dedicated funds for the yearly update and both phases of this project.

Distinction between one-time and on-going costs

None

Effects of non-funding

The agency would continue to violate the Local Government Accounting Statute, continue to receive audit findings and place the agency and its executives at risk of legal action.

If the revenues for the Electrical Account, Pressure Systems Safety Account and the Asbestos Account are not transferred back from the General Fund, the agency may be required to reduce expenditures and service delivery or increase fees above the fiscal growth factors. These actions may be necessary to ensure an adequate fund balance within the programs.

Expenditure Calculations and Assumptions

See attached summary of the Cost Allocation model. The model is available upon request.

The Workers Compensation Trust non-appropriated funds are included in the model for activities that are allocated based on total expenditures. The impact on those funds was totaled and then split evenly between the Medical Aid and Accident Funds. This percentage is based on the long-time practice of funding worker compensation-related administrative costs in this manner.

	FY 2006	FY 2007	TOTAL Biennium	Biennium 2007-2009	Biennium 2009-2011	TOTAL
FTEs	0.0	0.0	0.0	0.0	0.0	0.0
Objects of Expenditure:						
A - Salary and Wages	0	0	0	0	0	0
B - Employee Benefits	0	0	0	0	0	0
C - Pers Svc Contracts	0	0	0	0	0	0
E - Goods and Services	0	0	0	0	0	0
G - Travel	0	0	0	0	0	0
J - Capital Outlays	0	0	0	0	0	0
TOTAL Expenditures	\$0	\$0	\$0	\$0	\$0	\$0
Funds:						
001-General Fund	0	0	0	0	0	0
02V-PSEA	0	0	0	0	0	0
095 Electrical	0	0	0	0	0	0
608 Accident Account	0	0	0	0	0	0
609 Medical Aid Account	0	0	0	0	0	0
Other	0	0	0	0	0	0
TOTAL Funds	\$0	\$0	\$0	\$0	\$0	\$0

Implementation of Fiscal Year 2007 Supplemental Cost Allocation
Direct Cost Plus Allocated Cost - Results by Fund

Agency Total

Fund		Planned Expenditures (Enacted-Appropriated and Non-appropriated)	Impact of Yearly Update	Expenditures in FY 06 & FY 07
001	General Fund State	\$15,202,000	\$13,000	\$15,215,000
02V	PSEA	\$37,277,000	\$139,000	\$37,416,000
03B	Asbestos	\$808,000	\$0	\$808,000
095	Electrical	\$34,743,000	\$122,000	\$34,865,000
162	Farm Labor	\$28,000	\$3,000	\$31,000
163	Right to	\$1,836,000	(\$17,000)	\$1,819,000
234	Public Works	\$2,664,000	\$256,000	\$2,920,000
885	Plumbers	\$1,577,000	\$12,000	\$1,589,000
892	Pressure Vessel	\$3,324,000	\$23,000	\$3,347,000
	Workers Comp Trust	\$427,415,000	(\$551,000)	\$426,864,000
	BLS Federal Grant	\$208,000	\$0	\$208,000
	<i>TOTAL</i>	<i>\$525,082,000</i>	<i>\$0</i>	<i>\$525,082,000</i>

Implementation of Fiscal Year 2007 Supplemental Cost Allocation
Direct Cost Plus Allocated Cost - Results by
Administration
Program 010

Fund		Planned Expenditures (Enacted – Appropriated and Non-appropriated)	Impact of Yearly Update	Expenditures in FY 06 & FY 07
001	General Fund State	\$512,000	\$34,000	\$546,000
02V	PSEA	\$438,000	\$38,000	\$476,000
03B	Asbestos	\$38,000	\$2,000	\$40,000
095	Electrical	\$1,211,000	\$40,000	\$1,251,000
162	Farm Labor	\$0	\$1,000	\$1,000
163	Right to	\$106,000	(\$13,000)	\$93,000
234	Public Works	\$103,000	\$11,000	\$114,000
885	Plumbers	\$58,000	\$2,000	\$60,000
892	Pressure Vessel	\$120,000	\$3,000	\$123,000
	Workers Comp Trust	\$40,888,000	(\$118,000)	\$40,770,000
	BLS Federal Grant	\$208,000	\$0	\$208,000
	<i>TOTAL</i>	<i>\$43,682,000</i>	<i>\$0</i>	<i>\$43,682,000</i>

Implementation of Fiscal Year 2007 Supplemental Cost Allocation
Direct Cost Plus Allocated Cost - Results by Fund
Information Services
Program 030

Fund		Planned Expenditures (Enacted - Appropriated Non-appropriated)	Impact of Yearly Update	Expenditures in Y 06 & FY07
001	General Fund State	\$942,000	\$185,000	\$1,127,000
02V	PSEA	\$968,000	\$92,000	\$1,060,000
03B	Asbestos	\$18,000	(\$2,000)	\$16,000
095	Electrical	\$1,804,000	\$70,000	\$1,874,000
162	Farm Labor	\$0	\$0	\$0
163	Right to	\$287,000	(\$4,000)	\$283,000
234	Public Works	\$24,000	\$89,000	\$113,000
885	Plumbers	\$78,000	\$9,000	\$87,000
892	Pressure Vessel	\$174,000	\$19,000	\$193,000
	Workers Comp Trust	\$77,002,000	(\$458,000)	\$76,544,000
	BLS Federal Grant	\$0	\$0	\$0
	<i>TOTAL</i>	<i>\$81,297,000</i>	<i>\$0</i>	<i>\$81,297,000</i>

Implementation of Fiscal Year 2007 Supplemental Cost Allocation
Direct Cost Plus Allocated Cost - Results by
Legal Services
Program 090

Fund		Planned Expenditures (Enacted - Appropriated and Non-appropriated)	Impact of Yearly Update	Expenditures in FY 06 & FY 07
001	General Fund State	\$441,000	(\$206,000)	\$235,000
02V	PSEA	\$151,000	\$9,000	\$160,000
03B	Asbestos	\$0	\$0	\$0
095	Electrical	\$382,000	\$12,000	\$394,000
162	Farm Labor	\$0	\$2,000	\$2,000
163	Right to Know	\$2,000	\$0	\$2,000
234	Public Works	\$0	\$156,000	\$156,000
885	Plumbers	\$24,000	\$1,000	\$25,000
892	Pressure Vessel	\$14,000	\$1,000	\$15,000
	Workers Comp Trust	\$40,114,000	\$25,000	\$40,139,000
	BLS Federal Grant	\$0	\$0	\$0
	<i>TOTAL</i>	<i>\$41,128,000</i>	<i>\$0</i>	<i>\$41,128,000</i>